

# FDIC State Profile

Summer 2004

## Massachusetts

Economic conditions in Massachusetts show some improvement as employment conditions begin to stabilize.

- According to official payroll estimates, Massachusetts has yet to experience sustained employment growth during recent months however the decline in employment has ended.
- The state's unemployment rate has fallen from 5.9 percent at year-end 2003 to 4.8 percent in April 2004, the lowest unemployment level since December, 2001.

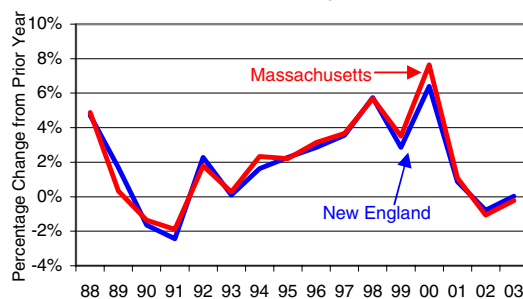
**Personal income levels remain third highest in the nation despite minimal growth.**

- Massachusetts shows a striking difference in its national ranking for level of personal income compared to changes in those levels. In terms of the *level* of personal income per capita, Massachusetts has been among the highest in the country, trailing only Connecticut and New Jersey. In terms of the *rate of growth*, however, Massachusetts was the slowest in the country.
- The 2001 recession, like the 1990-1991 recession, resulted in large changes in real (inflation-adjusted) personal income per capita in the state (See Chart 1). Following a moderate decline in annual real per capita income during 2002, conditions stabilized in 2003.
- Income levels in Massachusetts remain very impressive. Per capita income during 2003 was one-quarter higher than the national average and marginally above the New England average (See Chart 2). Perhaps even more striking, *all* of the top six states in terms of levels of per capita income were located in FDIC's New York Region, encompassing the Northeast as well as Maryland and the District of Columbia.

**Population growth in Massachusetts continues to lag the Nation.**

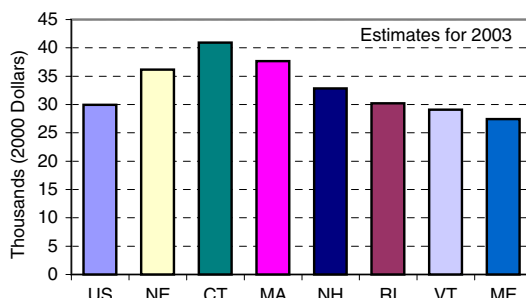
- Population growth in Massachusetts has been slow, about the same as New England and only slightly more than one-half of the growth in the United States (See Chart 3). According to New England Economic Partnership estimates, population growth is expected to remain very modest over the years ahead while growth in real personal

Chart 1: Real Per Capita Personal Income Patterns Mirror New England Trends



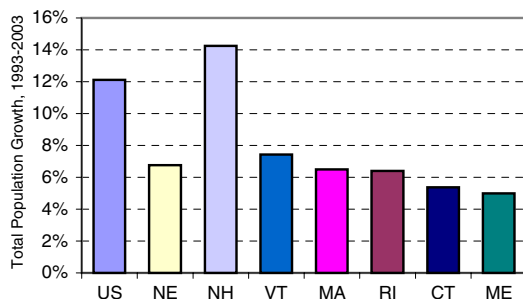
Source: Bureau of Economic Analysis, Haver Analytics

Chart 2: Massachusetts' Real Per Capita Personal Income Is the Second Highest in New England



Source: Bureau of Economic Analysis, Haver Analytics

Chart 3: Population Growth Has Been Near the New England Average Over the Past Ten Years



Source: Bureau of the Census, Haver Analytics

## State Profile

income per capita should return to approximately its long-term (fifteen-year) average.

### Net interest margin compression continues to affect earnings.

- Massachusetts' community institutions<sup>1</sup> continue to be profitable,<sup>2</sup> despite pressure from declines in net interest income (See Table 1). Earnings have been affected by a decline in net interest margins associated with the low interest rate environment as yields on earning assets have declined faster than funding costs. Funding costs are historically low and may have reached effective floors.
- Community institutions have also seen a 15-basis point decline in noninterest income to average assets in the first quarter of 2004. This decrease was not offset by an improvement in operating efficiencies.

### The number of branches remained relatively stable in Massachusetts, while out-of-state ownership increased.

- In 1994, there were 1,968 branches of insured financial institutions in Massachusetts with only 12 branches operated by insured institutions headquartered out-of-state. In 2003, the total number of branches increased to 2,090 with the number owned by institutions based elsewhere increasing to 637 (See Chart 4).
- Deposits in branches in the state increased from \$100 billion in 1994 to \$172 billion in 2003. During the same period, total deposits of institutions headquartered in Massachusetts increased from \$118 billion in 1994 to \$148 billion in 2003.

### Interest rate risk remains a concern for Massachusetts' institutions as concentrations of fixed-rate, long-term assets continue to increase.

- The conventional 30-year mortgage rate has declined significantly over the past several years and is still historically low. According to the Mortgage Bankers Association, on a national basis, the level of adjustable rate mortgages has increased from only about 13.5 percent of originations in December 2002 to almost 28 percent as of March 2004. While this ultimately may allow insured institutions to reprice assets more quickly, they still hold large volumes of long-term assets with low fixed rates.
- Since the late 1990s, asset maturities lengthened at many institutions, moderated slightly in late 2002 and early 2003, and increased again during the first quarter of 2004.

<sup>1</sup>Insured institutions with assets less than \$1 billion, excluding institutions less than three years old and specialty institutions.

<sup>2</sup>In 2003, Massachusetts assessed back taxes on REITs that were previously thought to be exempt in the state. This development is expected to be a one-time event, as several years worth of taxes were assessed at that time. Going forward, however, insured institutions maintaining REITs may expect to pay an incremental amount more in taxes for REITs.

With the large volume of long-term assets on the books, some insured institutions may be faced with a mismatch of asset and liability repricing. Net interest margin may compress if short-term interest rates increase, as liabilities reprice at a faster rate than assets (See Chart 5).

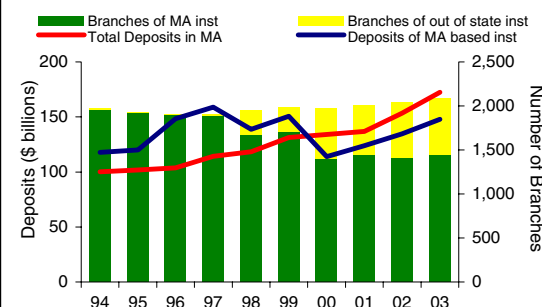
- The extension of asset maturities is pronounced in the state, reflecting the large percentage of thrifts and residential lenders. Savings institutions represent 82 percent of insured institutions in Massachusetts, and residential real estate loans comprised almost 58 percent of their average loan portfolio as of March 31, 2004.

**Table 1: Earnings Hampered by Net Interest Margin Compression**

| Percentage of Average Assets | First Quarter |      | Basis Point Change |
|------------------------------|---------------|------|--------------------|
|                              | 2003          | 2004 |                    |
| Net Interest Income          | 3.45          | 3.39 | -0.06              |
| Total Noninterest Income     | 0.71          | 0.56 | -0.15              |
| Noninterest Expense          | 2.82          | 2.80 | -0.02              |
| Provision Expense            | 0.06          | 0.04 | -0.02              |
| Security Gains & Losses      | 0.13          | 0.13 | 0.00               |
| Income Taxes <sup>2</sup>    | 0.79          | 0.45 | -0.34              |
| Net Income (ROA)             | 0.62          | 0.80 | 0.18               |
| Net Interest Margin (NIM)    | 3.71          | 3.65 | -0.06              |

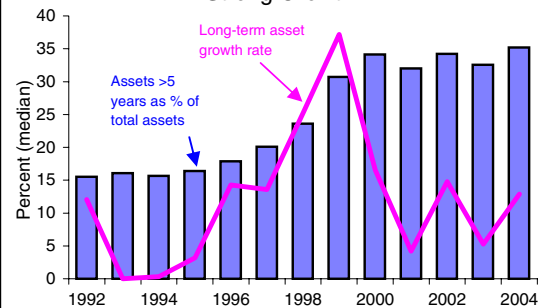
Source: Bank and Thrift Call Reports. Aggregate data for institutions with assets <\$1 billion. Excludes specialty institutions and de novos.

**Chart 4: Number of Branches Stable but Out-of-State Ownership Increasing**



Source: Summary of Deposits. Data as of 2nd quarter.

**Chart 5: Long-Term Assets Still Exhibiting Strong Growth**



Source: Bank Call Reports, Data as of 1st quarter.

## Massachusetts at a Glance

| <b>General Information</b>                 | <b>Mar-04</b>     | <b>Mar-03</b> | <b>Mar-02</b>  | <b>Mar-01</b>   | <b>Mar-00</b> |
|--|-------------------|---------------|----------------|-----------------|---------------|
| Institutions (#)                           | 207               | 214           | 219            | 227             | 228           |
| Total Assets (in thousands)                | 217,299,066       | 197,467,131   | 180,404,625    | 173,374,938     | 153,764,229   |
| New Institutions (# < 3 years)             | 2                 | 3             | 2              | 3               | 2             |
| New Institutions (# < 9 years)             | 3                 | 4             | 5              | 7               | 6             |
| <b>Capital</b>                             | <b>Mar-04</b>     | <b>Mar-03</b> | <b>Mar-02</b>  | <b>Mar-01</b>   | <b>Mar-00</b> |
| Tier 1 Leverage (median)                   | 9.37              | 9.08          | 9.20           | 9.46            | 9.75          |
| <b>Asset Quality</b>                       | <b>Mar-04</b>     | <b>Mar-03</b> | <b>Mar-02</b>  | <b>Mar-01</b>   | <b>Mar-00</b> |
| Past-Due and Nonaccrual (median %)         | 0.71%             | 0.91%         | 0.81%          | 0.89%           | 0.99%         |
| Past-Due and Nonaccrual >= 5%              | 1                 | 3             | 6              | 5               | 5             |
| ALLL/Total Loans (median %)                | 1.00%             | 1.01%         | 1.00%          | 0.98%           | 0.98%         |
| ALLL/Noncurrent Loans (median multiple)    | 4.51              | 4.79          | 4.50           | 4.33            | 3.30          |
| Net Loan Losses/Loans (aggregate)          | 0.08%             | 0.14%         | 0.14%          | 0.08%           | 0.04%         |
| <b>Earnings</b>                            | <b>Mar-04</b>     | <b>Mar-03</b> | <b>Mar-02</b>  | <b>Mar-01</b>   | <b>Mar-00</b> |
| Unprofitable Institutions (#)              | 7                 | 18            | 4              | 7               | 3             |
| Percent Unprofitable                       | 3.38%             | 8.41%         | 1.83%          | 3.08%           | 1.32%         |
| Return on Assets (median %)                | 0.70              | 0.69          | 0.81           | 0.78            | 0.90          |
| 25th Percentile                            | 0.47              | 0.35          | 0.64           | 0.54            | 0.62          |
| Net Interest Margin (median %)             | 3.46%             | 3.59%         | 3.71%          | 3.60%           | 3.70%         |
| Yield on Earning Assets (median)           | 5.03%             | 5.60%         | 6.42%          | 7.43%           | 7.28%         |
| Cost of Funding Earning Assets (median)    | 1.56%             | 2.00%         | 2.74%          | 3.86%           | 3.55%         |
| Provisions to Avg. Assets (median)         | 0.02%             | 0.03%         | 0.04%          | 0.04%           | 0.03%         |
| Noninterest Income to Avg. Assets (median) | 0.39%             | 0.48%         | 0.40%          | 0.39%           | 0.34%         |
| Overhead to Avg. Assets (median)           | 2.68%             | 2.70%         | 2.62%          | 2.66%           | 2.66%         |
| <b>Liquidity/Sensitivity</b>               | <b>Mar-04</b>     | <b>Mar-03</b> | <b>Mar-02</b>  | <b>Mar-01</b>   | <b>Mar-00</b> |
| Loans to Deposits (median %)               | 75.06%            | 72.94%        | 76.86%         | 80.59%          | 81.50%        |
| Loans to Assets (median %)                 | 61.15%            | 59.84%        | 62.43%         | 64.46%          | 65.96%        |
| Brokered Deposits (# of Institutions)      | 24                | 19            | 12             | 15              | 15            |
| Bro. Deps./Assets (median for above inst.) | 1.81%             | 1.42%         | 1.22%          | 1.01%           | 0.55%         |
| Noncore Funding to Assets (median)         | 17.83%            | 16.82%        | 16.69%         | 16.02%          | 15.07%        |
| Core Funding to Assets (median)            | 70.26%            | 71.63%        | 72.15%         | 72.43%          | 72.73%        |
| <b>Bank Class</b>                          | <b>Mar-04</b>     | <b>Mar-03</b> | <b>Mar-02</b>  | <b>Mar-01</b>   | <b>Mar-00</b> |
| State Nonmember                            | 23                | 24            | 26             | 28              | 28            |
| National                                   | 12                | 13            | 12             | 12              | 13            |
| State Member                               | 2                 | 2             | 2              | 2               | 2             |
| S&L  | 6                 | 6             | 6              | 7               | 7             |
| Savings Bank                               | 15                | 15            | 15             | 14              | 15            |
| Stock and Mutual SB                        | 149               | 154           | 158            | 164             | 163           |
| <b>MSA Distribution</b>                    | <b># of Inst.</b> | <b>Assets</b> | <b>% Inst.</b> | <b>% Assets</b> |               |
| Boston MA-NH PMSA                          | 118               | 180,503,555   | 57.00%         | 83.07%          |               |
| No MSA                                     | 18                | 6,282,057     | 8.70%          | 2.89%           |               |
| Worcester MA-CT PMSA                       | 15                | 4,603,486     | 7.25%          | 2.12%           |               |
| Springfield MA                             | 13                | 7,236,685     | 6.28%          | 3.33%           |               |
| Brockton MA PMSA                           | 9                 | 1,757,222     | 4.35%          | 0.81%           |               |
| Lawrence MA-NH PMSA                        | 8                 | 1,535,591     | 3.86%          | 0.71%           |               |
| Pittsfield MA                              | 7                 | 2,744,810     | 3.38%          | 1.26%           |               |
| Providence-Fall River-Warwick RI-MA        | 6                 | 4,457,587     | 2.90%          | 2.05%           |               |
| Lowell MA-NH PMSA                          | 5                 | 1,794,723     | 2.42%          | 0.83%           |               |
| Fitchburg-Leominster MA PMSA               | 4                 | 736,399       | 1.93%          | 0.34%           |               |
| New Bedford MA PMSA                        | 2                 | 4,004,862     | 0.97%          | 1.84%           |               |
| Barnstable-Yarmouth MA                     | 2                 | 1,642,089     | 0.97%          | 0.76%           |               |